RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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June 29, 1988 **LETTER 994**

June 17 DJIA 2104.02; PTI 2730; A-D Ratio -8.86
June 24 DJIA 2142.96; PTI 2735; A-D Ratio -8.51
Current Dow Yield: 3.49%; Dow P/E: 14.8
Dow 200-day mov aver: 2055; DowPow: 987

THE DOLLAR: A month ago the Dollar Index rallied above a three-year declining channel, a move which sent the September Dollar Index futures contract to 92. The Index declined slightly, then last week the Index rallied over 94. The dollar has finally turned bullish, looking stronger now than at any time since 1985.

THE MARKET: This is not the most auspicious time to publish, since there are a number of critical market divergences that may or may not be resolved by the time you receive this report. But Wall Street doesn't arrange itself in harmony with Richard Russell's deadlines, so here goes.

Immediately after Black Monday I wrote that "market crashes are rare birds, but the surest action in the market is the action that follows a crash." That action, I stated, is an almost automatic recovery of 50% of the ground lost. On this basis the Dow could be expected to correct half of the bear market losses from the August high to the October crash low, a correction that could take the Dow back to 2230.

Up to this point, the action of the market, and more specifically that of the Dow, has been so laggard that the "automatic" recovery thesis has almost been forgotten. Yet my PTI keeps pushing ahead. The PTI's persistent rallying keeps alive the possibility of a full 50% bear market recovery (back to around Dow 2230). Will it happen? History suggests that it "should." I think the action of DowPow (see later section) may provide the best hints.

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In the last Letter (see "Late Notes") I stated that since the Crash, the Dow has made five attempts to punch decisively through the 2150 area. These five efforts occurred successively on October 21, January 7, March 18, April 12, and most recently on June 15. The current effort is part of the upside attack that began in mid-June.

The technical background of the market during these five Dow attacks has been somewhat suspect. The reason is divergence -- on the part of both the Transportation Average and the advance-decline ratio. Remember that under Dow Theory only penetrations of preceding points by BOTH Averages are valid for predictive purposes. A penetration by a single Average, unconfirmed by the other, carries no forecasting value and is more apt than not to be deceptive.

To be specific, back on March 23 (with the Dow at its 2087.37 peak) the Transportation Average closed at 904.12. This was followed by a decline, and then a further attack on the highs. On June 22 the Dow closed at a new post-crash recovery high of 2152.20, but again the Transports failed to confirm. A confirmation would now require that the Transports close above 904.12 (i.e., above their closing high of three months ago). A persistent refusal by Transports to better the 904.12 level would be bearish and would suggest that a market top was forming.

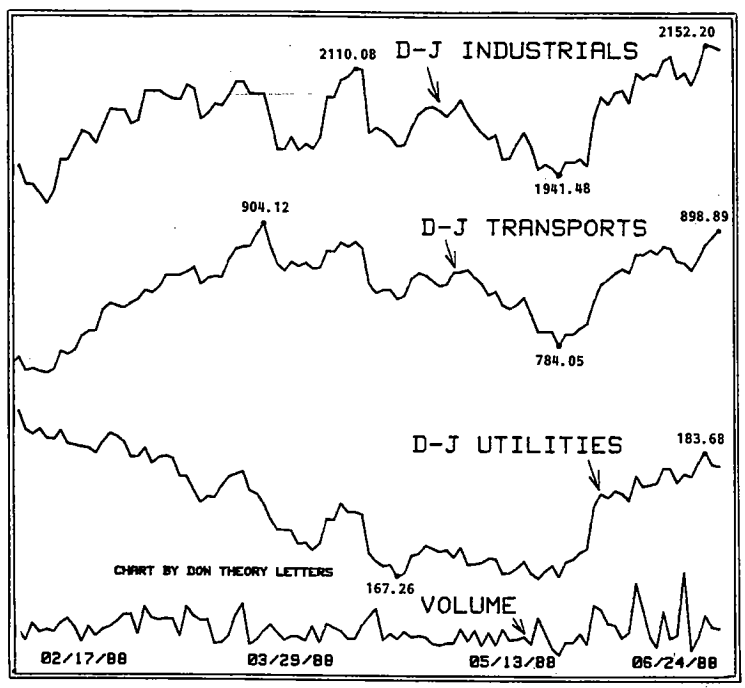
A comparable situation exists in the Dow/breadth relationship. In the face of the series of Dow attacks on the highs, the A-D ratio has recorded a series of three declining tops. The three declining tops occurred on March 17, April 12, and June 15 (they can be seen on the page 2 chart). This kind of divergence (we used to call it a "triple price/breadth divergence") has been the forerunner of many serious market declines. To erase the price/breadth divergence, the A-D ratio will have to better its March 17 level.

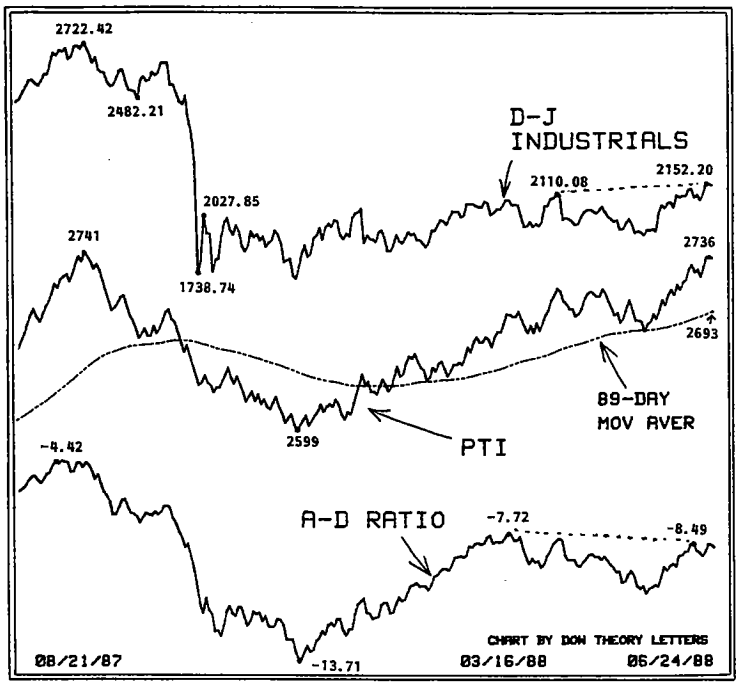
Unfortunately, as this is written I have no way of knowing whether these important divergences will be eliminated or not. However, there has been little mention of these divergences, and most advisors' attentions have been riveted on the Dow and the fact that it has bettered its 200-day moving average.

BIG PICTURE: For the benefit of new subscribers, I will repeat that this is a bear market, and it's a bear market that is still in its first phase. This is the phase where stocks go down for no obvious or apparent reason, and they go down in the face of continuing "good business." Because of this "mystifying" type of first phase action, amateur investors during the first phase often claim that Wall Street is "crazy" or that "the stock market makes no sense at all."

The second phase of a bear market sees stocks go down in response to obviously deteriorating business conditions. The second phase is usually the longest phase and the most deceptive one. It is here that one sees many stocks crash as earnings turn unexpectedly bad and as business conditions turn sour.

Bear markets are tricky and deceptive. No bear market in history has ever been satisfied with just one "whack" at the pocketbooks of investors and traders. The bear wants to do a complete job, and that entails getting in a number of costly shots at the nation's stockholders. In order to achieve this, the bear must do two things: (1) the bear has to convince the public (repeatedly) that "the worst is over" and that "this is the time to buy again." (2) And, of course, in order to do that the bear has to produce big, exciting stock





market rallies. Nothing is so calculated to turn the public bullish again as a nice, juicy 100-point rally in the Dow.

Now let's philosophize a bit. Take a deep breath and exhale slowly. Where the stock market is concerned, you have to learn to sit back, relax, and just let the market do its thing. You must give the market plenty of leeway. In a bull market this entails being fully invested, relaxing, sitting out the bumps and rolls, sitting tight through the reactions, staying with the main (primary) trend, and allowing the market to make money for you.

In a bear market the exact opposite action is required. In a bear market you have to sell your stocks, move to the sidelines, and hang tight through all the various rallies, violent advances, and bullish rumors. Above all, you must keep your long-term perspective. The person who has to trade every move, the guy who can't stand the Dow rallying 25 points without his "being in on it," the lady who craves action and excitement, these people will find that their various "needs" will be amply satisfied by Wall Street -- but usually through a series of frustrating and costly losses.

I have written repeatedly in Letter after Letter that I expect this to be a difficult and deceptive bear market. I said that I expected the government to "fight the bear with tooth and nail." And I warned that I felt that the bear market would be a long one -- perhaps lasting many years.

The more I see of this bear market, the stock action, the psychology of the public, the reactions of Washington -- the more convinced I am that my original instinct was correct. What was my instinct saying? It can be expressed in a single phrase -- "It ain't going to be easy!"

TECHNICAL COMMENTS: June 8: The Dow surged 48.36 points to close at 2102.95 and above its 200-day moving average for the first time since Black Monday. I don't know how or why it happens, but at various times Wall Street becomes obsessed with specific technical indicators. In my 40 years of watching the market I've seen Wall Street become obsessed with the odd-lots, the short sale ratio, the specialists' activities, the Confidence Index, Will-Go, insider buying (this obsession is still prominent today), brokers' loans, money supply, the leading indicators, the trade balance (evidently still today's obsession), and on and on. Through painful experience, I have learned to be skeptical of the "obsession of the day." *What everyone is watching ceases to be a factor in the stock market.*

Over the past few months everyone has been watching and talking about the 200-day moving average of the Dow. So when the Dow on June 8 rallied above its 200-day moving average, I had the feeling that every technician and every technically-minded trader and every switch-fund operator jumped in and bought stocks. Almost overnight, sentiment regarding the stock market turned bullish, and many gurus announced that "a new bull market" had been signaled.

In bear markets it is not at all unusual to see the Dow and the major indices climb temporarily above their moving averages. I take such action, not as a bull signal, but simply as evidence that the market has become overly enthusiastic and technically "over-bought." (And I might add that those who have been trading the market on the basis of the 200-day moving averages have probably been whip-sawed a few times already in this bear market.)

MOVEMENT'S END: According to Dow Theory, a movement ends at the point where the two Averages (Industrials and Transports) record their last confirmed highs or lows. The last confirmed highs of the post-crash rally were recorded on March 23, at which point the D-J Industrials and Transports recorded their last joint post-crash highs. All the upside progress since March 23 has been made by the Dow alone. The Transports have remained BELOW 904.12.

So as I stated earlier, let's relax, let's check our greed, let's watch the action. Let's see if the Transports can keep the rally going in which case they'll have to climb above 904.12. If the Transports can't do that, this market will be in trouble.

Question: On June 15 many of the other major indices and averages advanced to post-crash highs. Isn't that important? Doesn't that suggest that we're in a bull market?

Answer: Over and over again I've seen where a non-confirmation by the D-J Industrial Average or Transportation Average will signal a major turn in the market, regardless of what any other average or indicator is doing. No, the refusal of the D-J Transportation Average to confirm the recovery high in the Dow is extremely significant. Furthermore, the longer the time which elapses without a Transportation confirmation, the less are the chances that such a confirmation will materialize.

Question: Why did you make that last statement about elapsed time without a confirmation?

Answer: Because in a primary bear market both business conditions and stock values will deteriorate through time. Remember, the 1988 high in the Transporation Average was recorded three months ago on March 23. As the weeks go by the background conditions of business are deteriorating and the values of the 20 stocks that make up the D-J Transportation Average are diminishing. This deterioration in values as the bear market drags on lowers the odds that the Transports will confirm.

Question: In the June 15 *Wall Street Journal* (front page) it was reported that "Fewer economists see a recession coming soon. Just 54% of economists polled by Blue Chip Economics Indicators predict a recession by the end of 1989. Some 12% say it won't arrive until at least 1991."
In other words, top economists are growing more optimistic. In view of this, how can you argue that a bear market is in force?

Answer: My own opinion is that the majority of economists are going to be wrong. I don't believe the August 1987 top, the bear signal, and the October 19 crash came out of an economic vacuum. If I had to guess I'd guess that the trouble, when it arrives, will come from an unexpected source, a sector where the economists are NOT now looking.

Also, there is the matter of timing. There is no law that states that once the primary trend of the stock market turns down, the economy must turn down within three months or six months or a year. The longest lead time (since WW II) from the market top to

the downturn of the economy occurred in 1976 when the market topped in November '76 and the economy turned down 13 months later -- in December 1977. If that lead time was to hold in the current situation, we could expect the economy to hit its peak and turn down this September (13 months after the August market top). Time will tell, but as I said, there is no set time span between a stock market's top and the beginning of trouble in the economy.

Question: With our overseas debts continuing to accumulate and compound (as seen in the US current accounts deficit), do you think that the US will eventually just print money to pay its foreign creditors or do you think the US will take the pain of getting its house in order via high interest rates, a cutback in consumer spending, and a recession?

Answer: It is clear to me that no real action will be taken by the US until a crisis occurs. A crisis could occur any time that foreigners panic at the thought of the US ignoring its deficits -- or a crisis may come later when interest payments become too much for the US to handle.

Already, there have been rumors that the Japanese may demand yen-denominated Treasury bonds, but if such a demand is made you can be sure that it won't occur until after the elections (all problems are being held in abeyance until "after the elections").

It is obvious to me that the US will do anything rather than take a recession, and this can be seen in the gingerly manner in which the Fed has reacted to the rocketing CRB Commodities Index and the rising (even though temporary) inflationary forces. This period of economic expansion is now in its 67th month, and is the longest of this century (or since the record expansion of 1848 to 1853).

This has resulted in various economists announcing that trouble may be put off until the 1990s. One economist even states that the bond market is such a stabilizing and equalizing influence on the economy that recessions may have gone the way of the nickel cup of coffee. Russell opinion: Don't belive it, night still follows day and recessions will still follow booms -- the longer the economic expansion, the longer (or deeper) the eventual recession.

Question: Month after month people keep warning about trouble in the Japanese stock market. It never comes but what do you think?

Answer: I think Japan's market may finally be getting close to trouble. The Japanese market has taken over as the world's leading market, in total value, volume, P/E ratios, lowest yields. There's no question about it, Japan's market is vitally important to the world picture.

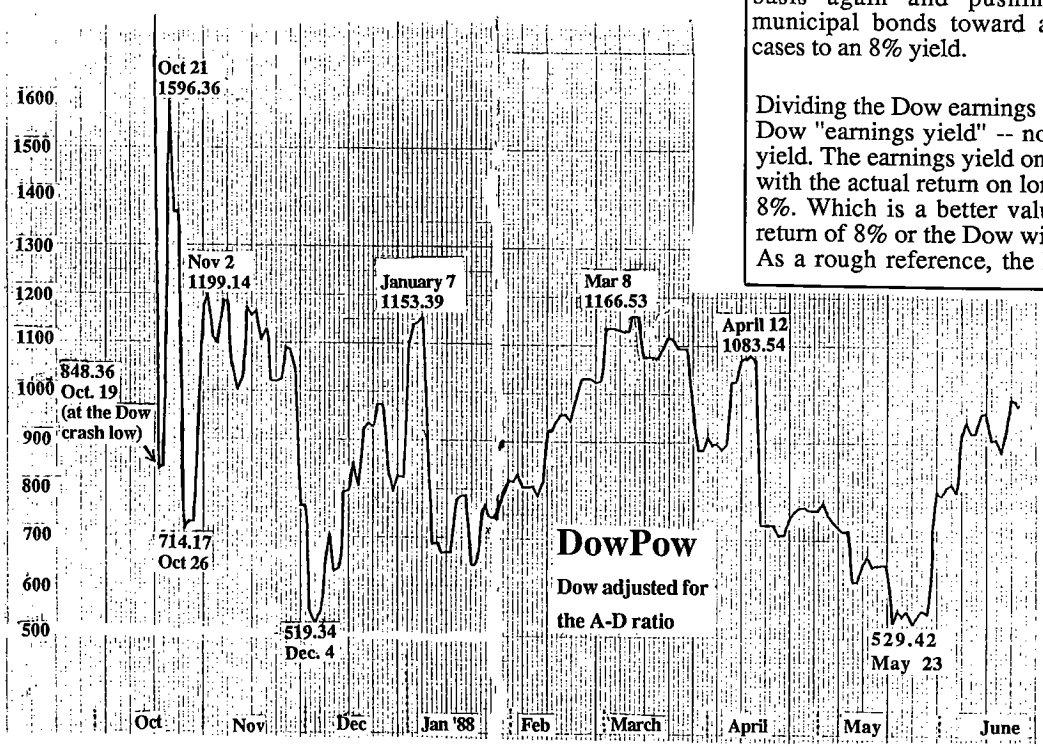
Stan Weinstein (*Professional Investor*) watches this market very closely, and he doesn't like what he sees, which is technical deterioration. Stan notes that many of the leading Japanese stocks and the broader Japanese stock average have not risen to new highs - even though the Nikkei did recently. He sees this as a danger signal, and Stan believes the Japanese stock market could crash. If it does, it will hardly be a plus for our own market. The Japanese hold roughly $16 billion of US stocks, which they could dump to raise cash if their market comes apart at the seams.

DOWPOW and the PTI: These are my two proprietary indices. The PTI tracks the trend, DowPow shows us the strength of the trend.

The PTI rallied above its 89-day moving average (see Letter 983) in late-January. This turned the PTI bullish, and it has remained bullish ever since, as seen on the page 2 chart. I have many subscribers who don't care about bull or bear markets, yields, or P/E ratios; they trade strictly on whether the PTI is bullish or bearish, and the PTI's consistent action has rendered this year an easy one for them.

DowPow is another story. It takes strong action in the Dow plus accompanying strong action in the A-D ratio to move DowPow. The daily chart indicates that we haven't had a consistent pattern of either since the crash. DowPow hit a bear market low of 519.34 on December 4. It hit a high of 1153.39 on January 7. DowPow has been fluctuating between those two levels ever since.

As recently as May 23, DowPow dropped to 529.42, but on the drop it held 10 points above its December 4 low. From there DowPow rallied to 990 on June 22. On the upside, DowPow's first real target is the 1153.39 peak of January 7. So far in 1988 the 1100-1200 area in DowPow has halted every market advance. We should know soon if this time it's different.



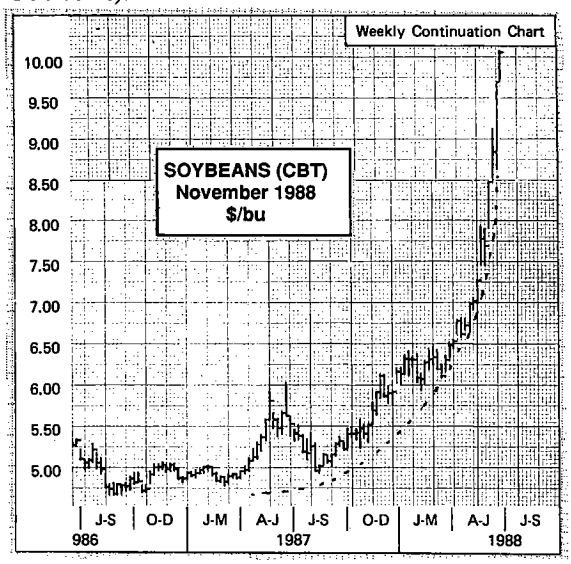
INVESTMENT POSITION: El Toro is in the box; and yes,it's a bear market. Interest rates have been heading up, pushing the T-bonds over the 9% yield basis again and pushing AA-rated municipal bonds toward and in some cases to an 8% yield.

Dividing the Dow earnings (144.45) by the Dow price gives us the Dow "earnings yield" -- not the dividend yield, but the earnings yield. The earnings yield on the Dow is now 6.87%. Compare that with the actual return on longer-term muni bonds which is around 8%. Which is a better value, the bonds with an actual tax-free return of 8% or the Dow with an earnings yield of a mere 6.87%? As a rough reference, the Dow earnings yield and the yield on long-term T bonds should be about equal (at which point the Dow is a good value).

At any rate, we're moving slowly but surely toward trouble in the economy, which is the real reason why the market is stalling here and why the Dow is still 600 points below its bull market high. In view of this, my advice continues to be, "Stay away from stocks," which is just another way of saying -- respect the bear. I continue to feel that top-rated bonds (including T-bonds) offer value, attractive yields, and a

good deal of safety. Everyone is worried about inflation. I don't see inflation as a long-term worry, I see deflation as the real long-term worry. Top-rated bonds tend to do well in deflationary times.

COMMODITIES: Only three times in this century has the US experienced both extreme drought and extreme heat. This is one of those times. As a result, a large portion of the food crops of the nation are going to be burned up, destroyed. This has led to a "weather bull market" and a big one. This weekly chart of soybeans (courtesy of *Dunn & Hargitt*) show the beans in a parabolic climb, set off by day after day of "limit up" (the limit climb in a day for beans is 30 cents).



The grains are now rising in a parabolic curve pattern. It is the nature of the parabola to advance at an accelerating (geometric rate) until finally the advance approximates the vertical (in other words,the price action is straight up). It is also the nature of a parabolic curve to USE UP ALL THE BUYING POWER as it rises. At the top, the movement is EXHAUSTED. Finally, no one knows when the vertical stage of the parabolic curve will end, but when it does end, that's it -- you've seen a major top. Usually the price will not come back to the parabolic high for many years.

We remember the parabolic rise in gold in 1980. We remember the parabolic rise in the Dow during 1982 to '87. Now we see it in beans, corn, wheat (copper's parabolic rise ended last January).

More often than not, following the extreme high in the parabola, the price movement will come down violently or even crash. So that is what I believe we can look forward to in the grains. It can be a heck of a rise to the top, but don't get caught on the other side.

RESPONSIBILITY: I'll admit it, my favorite hobby is thinking (I guess reading comes in second). I've always been fascinated by ideas, and I like to ponder how the world turns and what works and what doesn't work.

I read eight newspapers a day, and the overwhelming impression that comes across as I read these newspapers is that the world is in a pretty chaotic state. I don't mean to imply that the world is more chaotic now than it was say 10 years ago or 50 years ago. I'm just saying that there's a lot of chaos out there -- so much that sometimes I honestly don't know how mankind carries on (somehow, it does, of course).

I read about the gangs, the drugs, the violence, the wars, the revolutions, the unpayable debts, the starvation, the child abuse, the divorces, the diseases, the poverty, and I wonder how all these horrendous problems can ever be solved. And more and more I'm coming to the conclusion that the only way they'll ever be solved is by people (individuals) taking responsibility for their own lives. That may take 50 years or 5,000 years, but I honestly can't envision any other way.

Dr. Frederick Perls, the late great founder of Gestalt psychology, wrote a good deal about responsibility. Perls referred to responsibility as response-ability, the ability of an individual to respond sanely and correctly to a given situation. And I believe that Perl's formula is the only hope for mankind -- the only hope for mankind to solve all its problems.

For instance, the drug problem (in my opinion) will only be solved when men and women individually decide that they will not use drugs. It's really a personal problem -- and solution -- in that the day all Americans give up drugs, the problem will cease to exist.

The same thing pertains to debt. The day most Americans decide to balance their own finances, to start saving, to vote spendthrift politicians out of office, to take the extreme pain of whittling down and then eliminating the federal debt, the day that happens, the debt fiasco will be over and the US will be on the rising-power path again.

Yes, it's the individual's ability and willingness to take his own life into his own hand, to live sanely, to vote sanely, to act sanely, that constitutes the ultimate salvation of mankind. If there is no individual responsibility, there is no hope. This I firmly believe.

On the great seal of the United States (it's printed on your dollar bill), you'll see the words, "Annuit Coeptis." This is, of course, Latin, and it means, "He has prospered our undertaking (or beginnings)." The "he" is God, and the "undertaking" is the miraculous concept of the United States of America. The founders of this nation represented probably the greatest group of political, social, and economic geniuses ever gathered together in one spot at one time. These men saw the US as a wondrous experiment in government. These men abhorred debt, they abhorred tyranny, and they fashioned a Constitution that was based on a system of safeguards and checks, safeguards so that no one group and no one branch of government could control or seize power over the nation.

These men knew that unlimited debt leads to economic slavery, and they knew that unlimited political power leads to social slavery. Therefore, they warned in the strongest terms against both.

But again I come back to individual responsibility. The US system of democracy is based on the will of the majority. Sidney Hook, my great teacher at New York University, said that democracy implies that it is the right of the people to make (and learn from) their own mistakes (not the mistakes of dictators and tyrants, but their own mistakes). I never forgot those words. Responsible people make mistakes, but they also learn from them. They learn to respond and react to their mistakes. In that course of action lies the ultimate hope for mankind.

NOTES & QUOTES: The bear market has hit Wall Street hard. Except for the big boys in the mergers and acquisitions follies or the hot shots in the boutiques, Wall Street (i.e., the retail brokers) is in a semi-depression. Listen to these quotes (courtesy of *Financial World,* June 28): "There's no more retail business, and if you think there is you're insane. There's no more syndicate business. Nothing is out there but discounted commisions, and the retail guy can't live off that. Registered reps are a thing of the past. Dead animals." That's from *Gruntal's* Ed Cuffe. This from a *Smith Barney* VP: "I'm down about 40% myself. But I'm here 20 years. I'll weather this thing. The young guys are doing nothing -- 10% of what they should be doing. They can't afford to live, and we can't afford to pay them. One or two months draw. Then one or two months' recoverable draw and that's it." This from a *Kidder, Peabody* broker: "There are only two ways a broker can make good money right now. Get in on a takeovear deal and ride it right. But then he has to know something he shouldn't know. Or move to another firm for a big fat wad up-front. Other than that, there's not much a broker can do today."

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While all eyes are on the trade (or the exchange of goods) deficit, few are paying attention to the much broader current accounts

deficit, which measures all exchanges of money. Sample item: During the first quarter foreigners earned $655 million more on their US investments than US investors did on foreign accounts. This was the first US interest-payments deficit since 1958 when the Commerce Dept. started keeping the records. The full current accounts deficit for the first quarter widened to $39.8 billion from $33.5 billion in the fourth quarter of 1987. The TOTAL INDEBTEDNESS of the US (to foreigners) at the end of '86 was $263 billion, and will probably rise to $400 billion at the end of '87. This is quadruple the foreign indebtedness of Brazil, the previous debt leader. Foreigners continue buying US businesses and shipping the profits back home, and this process will further affect the current accounts deficit. Thus, the "cheap dollar" may not be such a blessing after all.

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The Russian switch towards "glasnost" and "perestroika" and the Russian implied admission that the economics of Communism don't work has thrown the rest of the Red world into a tizzy. The latest upheaval comes from Vietnam, whose leaders now want to the bury the hatchet with the US and (of course) borrow money from us. Recently, Vietnam's Foreign Minister Nguyen Col Thach stated (in a *USA Today* Interview): "Charity is not working. We are too romantic. We have taught that everything from capitalism is corrupt. This is false. Without capitalism, there would be no socialism. Now, people who work very hard receive the same salary as the lazy ones. We are very good dreamers, but this is bad economics."

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According to *Fortune* magazine's statistics, 20 million Americans smoke marijuana, nearly 6 million regularly use cocaine and half a million are addicted to heroin. Said Francis Keating, assistant secretary for drug enforcement for the Treasury Dept., "Any industry with 25 million American consumers can support an enormous empire." The empire Keating is referring to, of course, is the drug empire centered in Medellin, Columbia.

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Ross, save us! The Post Office has just hired billionaire Ross Perot to help it solve its spiraling expense problems (and, of course, the PO's problems are your and my expenses). Here's what Perot is facing: The PO workers spends $2.2 billion a year for transportation alone, and its workers average (get this) $38,751 a year including overtime and benefits, which ranks them as the highest paid semi-skilled workers in the world. Good luck, Ross, you're tackling the ultimate horror -- big bureaucracy plus big unions.

The PO, with sales of a whopping $36 billion, spends a pitiful $11.6 million on research, a mere 0.03% of sales. No other corporation could survive with that minuscule research effort. In 1971 the PO was turned into a quasi-public corporation, and there is therefore no political accountability. According to John Crutcher, the postal-rate commissioner, "There are no stockholders' interests to protect. No problem of a hostile tender offer." Russell solution: Sell it to private interests, there's no other way. Unless, of course, Ross Perot can do something with this biggest of all dinosaurs.

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Lee Iacocca's first book had the publishing fraternity gasping as it sold an astounding 6.5 million copies. Now his second book, "Talking Straight" is out, and it promises to be a blockbuster as well. Here's an excerpt: "I see billions of dollars tied up in new corporate debt to keep the raiders at bay while research and development goes begging. I see billions going for greenmail, dollars that ought to be building new high-tech factories. I see confidence in Wall Street's integrity lower than at any time since the crash of '29. I also see a huge share of America's best management talent wasted on takeover games when it should be devoted to strengthening the industrial base of the country."

By the way, if you really want to know what's going on in America today, I heartily recommend two new "can't put 'em down" books that I'm reading simultaneously. And I mean these books are well-written, fascinating, informative,and eye-openers. The first is "The Predators' Ball -- The Junk Bond Raiders and the Men Who Stake Them," by Connie Bruck (Simon & Schuster). The second is "The Cocaine Wars" by Paul Eddy (Norton & Co.). Read them, they're important and terrific.

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The Russians are coming, and the times are a'changin'. San Diego is going to have a major Russian Art show and McDonalds heiress Joan Kroc has just contributed $1 million toward the show. I'm all for it. Cultural exchanges favor peace, while political and cultural isolation favor war.

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I don't know how many magazines I read each week, but one stands out above all the rest. It's the London *Economist*. I honestly don't know how they turn out such well-written, well-researched, informative articles every week. Each issue of the Economist includes a major, in-depth article about some aspect of the world (usually of the world economy). The June 11 issue featured a piece on "America's Capital Markets." I thought the article was both informative and brilliant, and I couldn't resist including this small section from the June 11 issue:

> ONE way to look at the financial condition of America in the summer of 1988 is to imagine the country as one vast leveraged buy-out. Like a company, it has built up huge debts, outpacing its equity. As is by now familiar, the United States has become the world's largest net debtor and is selling off its assets (factories, property, bonds) to foreigners in order to service its debts. Unlike most LBOs, however, the United States has continued to borrow as if there were no tomorrow. Which, if it carries on borrowing, there may not be.
>
> Increasingly, America's creditors are not private foreign investors (who have recently been net sellers of dollar securities) but foreign central banks seeking to support the dollar. According to *Grant's Interest Rate Observer*, on April 20th foreign central banks owned $229 billion of American Treasury securities. How long will they go on printing money to finance America's budget deficit? And, with that slice of America's debt, will they retain faith in the dollar as the world's reserve currency?
>
> If America's deficits remain high and foreigners become more reluctant to lend, then American interest rates will have to rise simply in order to attract funds. That, as in October, could spark off another crash as well as pushing the economy towards recession. Some argue that America can grow out of its foreign debt, earning enough to service it and to reduce the outstanding debt to a sustainable level. To run a trade surplus in the sufficiently long term to burn off this debt is certainly possible in theory. But it will not be easy, nor will it be without pain.
>
> America has another quite separate debt problem that needs to be taken into account. In the first quarter of 1988 the ratio of America's domestic non-financial debt to its nominal gross national product (GNP) reached 181.4%. No figure can be said conclusively to be unacceptable but this is indisputably high. After hovering at around the 140% level from 1940 to 1983, the debt load is again at levels not seen since the early 1930s when the economy collapsed.

* *

Financial World (June 28) lists the biggest money-makers on Wall Street for 1987. Five of the guys are listed as having made over $60 million, another 14 made over $20 million, and a third group of 13 made over $10 million. An incredible 48 people at Goldman Sachs made over $4 million with an unbelievable 26 of the Goldman fellows having made over $9.6 million. The winner overall -- Paul Tudor Jones II (Tudor Investments) who made between $80 and $100 million for the year.

* *

Canada, which has been choking on too much government, is finally deciding that capitalism is the way to go. Mark Skousen (*Forecasts & Strategies*, 7811 Montrose Rd., Potomac, MD 20854) notes that "there are several reasons for (Canada's) incredible turnaround. Canada's maximum tax on income has been reduced to 34%, and the capital gains rate has been shaved to an incredible 17.51% (on both short-term and long-term profits). Moreover, Canada has just adopted a remarkable C$500,000 lifetime

exemption on captial gains for Canadian citizens and residents. It must be taken over a 5-year period of time, but it's still quite a deal. This special benefit will go a long way in creating captial in Canada, the key to future economic growth." Russell comment -- this represents a tremendous and healthy reversal in Canadian economic philosopy. I've always said that if I had to live outside the US, the city I would move to would be Vancouver.

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I've written quite a bit about diamonds lately, and stones finally made the cover story of *Barron's,* June 13. The Central Selling Organization (owned by DeBeers) sells 90% of all the world's diamonds, and this cartel is so powerful that even the Russians pretty much abide by CSO rules (the Russians coordinate their diamond sales with the CSO).

Today, Japan (surprise) is the world's big buyer of diamonds, and therefore the CSO is increasingly gearing their "rough" (unpolished) diamond sales to the yen. After all, DeBeers doesn't want to give the Japanese, with their all-powerful yen, a free ride. Diamonds are sold for dollars by the CSO, but to adjust the rough diamonds to the yen, the CSO has been pushing diamond prices UP. Thus, in the last year, the No. 1 item on the Salomon Bros. list of various categories of assets is diamonds -- up 24.9%. And continued pressure from overseas markets is driving diamond prices still higher.

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Eurobonds are bonds issued by companies or government agencies outside of the jurisdiction of any country. Since "Euros" are beyond the scope of any regulators, they must of necessity be of high quality in order to sell (many Euros are issued by major US corporations). Eurobonds are generally exempt from any regulations or restrictions (they are bearer bonds). It is estimated that there are about $750 billion Euros floating around "out there" (including many non-dollar bonds). Turnover of Euros is around $13 billion a day.

Many Eurobond buyers purchase these bonds in custodial accounts via Swiss banks; it is estimated that 50% or more of all Euros are held in this way. Euros therefore provide tax-free income to their owners, and there may be no paper trail to the accounts. My guess is that many Americans hold vast amount of Eurodollar bonds in foreign accounts and collect tax-free interest. Of course, for US citizens this practice of collecting tax-free money without reporting it is illegal. According to US law, money collected by US citizens anywhere must be reported. But just imagine, for instance, how much dope money (Euros bought for hard cash) must now be sitting in Eurobonds, illegal money collecting tax-free interest for individuals with numbered accounts in Swiss or other banks.

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Last year 153 USA law enforcement officers were killed in the line of duty. That's down from 156 killed the year before and part of a downward trend over recent years. What's the reason -- soft-hearted criminals? Hardly. The reason is the trend toward officers wearing bullet-proof vests and carrying 15-shot automatics instead of 6-shot revolvers.

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The Tokyo Stock Exchange's newly-installed computer system has plenty of bugs, and it's driving Japanese brokers up the wall. The brokers are buying (for $14) special cloth baseball bats, and they vent their frustrations by beating the computers with the "soft" bats while shouting epithets.

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Newsweek (June 20) ran a cover story comparing Washington DC to NYC. A section by Joe Bob Briggs describes his view of DC life: "DC is the place where the American dream is really alive. That's the city where you start out sorting mail for an under-secretary of agriculture, jump over to the IRS to be head of misleading consumer information, move to Bethesda, get a transfer to Congress as an aide of your hometown representative, wait until he exposes himself in a public park, write a book about it and end up with your own show on CNN."

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GOLD, BONDS: Call me crazy, but I want to accumulate gold -- not gold shares, not gold certificates, not gold funds -- just gold. What I advise my subscribers to do, I do myself, and that means that I buy a fixed dollar amount of gold coins around the first of each month. Now if you want to accumulate an item, you're going to have mixed feelings about its price level. Once you have a fair quantity of the item (and I don't care if it's Tiffany lamps, baseball cards, or gold) part of you wants the price to go up (your assets are worth more), and part of you wants the price to go down (you can continue to accumulate at lower prices). That's the way I feel about the price of gold.

I really don't care if the metal goes up or down, because I'm going to continue buying Krugerrands or Maple Leafs or Coronas each month. Why keep buying? Instinct, a bit of greed, the wish to diversify -- and a definite feeling of comfort. Yeah, I find stacks of gold coins very comforting.

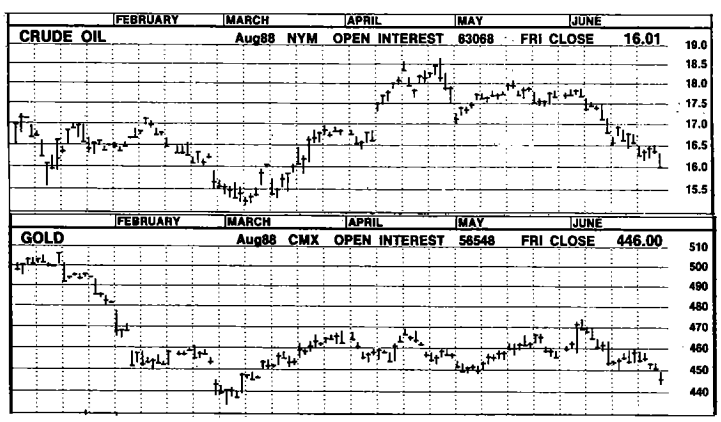
In this uncertain world where everything changes, where politicians keep changing the rules, where governments continue spending more than they take in, where citizens vote for an increasing amount of the "other guy's" income and assets, where the minimum wage keeps rising, where paper currencies buy less and less of real things, there's a definite comfort in owning something immutable, something of intrinsic value, something that will be money a year from now, a decade from now, a hundred years from now.

Everyone knows that the world is producing more gold. This year for the second year in a row, the US will actually produce more gold than Canada. Why then do men continue to search for gold? Why do new gold mines keep opening? The reason is that gold always has a market. There's a market for any quantity of gold at a price.

Won't the world produce too much gold? Yes, if the world starts shrinking its total supply of paper currencies. Will that ever happen? You've got to be kidding. That will happen when the world runs out of politicians, and I don't see that occurring in my lifetime.

Gold has been facing tough fundamentals lately. Oil is probably the single biggest item in the world inflation/deflation equation, and lately the price of oil has been weak. Last week spot crude closed at 16 bucks a barrel, and if anything that "low price" has deflationary overtones. A weather bull market has shot the price of grains through the roof, but that's a special situation, based on an act of God. All in all, aside from food, there doesn't seem to be any great inflationary push, and, in fact, the current decent bond market underscores the non-inflationary thesis.

These two charts of the August gold and oil contracts (courtesy of *Investor's Daily*) show the poor action of both crude oil and gold over the past few months. Oil is balanced on the psychologically important 16 dollar level. And gold has come down to test the March low in the 435 area. Oil should hold above 15, but if it doesn't there are going to be new deflationary problems in the Southwest and at the banks. Gold, if it doesn't hold 435, could test 420, although I expect 420 to hold. If 420 doesn't hold, gold will be a bigger price bargain than any of us gold-philes suspect.



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